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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA, EASTERN DIVISION

MARCELO CUNHA, Individually and on Behalf of All Others Similarly Situated,

Plaintiff,

vs.

HANSEN NATURAL CORPORATION, RODNEY C. SACKS, HILTON H. SCHLOSBERG, and THOMAS J. KELLY,

Defendants.

CASE NO. EDCV08-1249 SGL (JCx)
[Consolidated with EDCV08-1278 SGL (JCx)]

MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF DEFENDANTS' MOTION TO DISMISS THE CONSOLIDATED CLASS ACTION COMPLAINT

[Request for Judicial Notice Filed Concurrently Herewith]

Date: March 15, 2010
Time: 10:00 a.m.
Crtrm.: Hon. Stephen G. Larson

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I. INTRODUCTION

This is a lawsuit in search of a theory – a prime example of the type of abusive and meritless class action litigation that the Private Securities Litigation Reform Act ("PSLRA") was designed to cut off at the pleading stage.

In November 2007, Defendant Hansen Natural Corporation ("Hansen" or "the Company") announced its third-quarter results. Although Hansen reported record sales and profits, the results fell short of what most market analysts had been expecting, and Hansen's stock price fell. Some ten months later, this purported class action suit was filed, even though there had been no disclosure of fraud or other wrongdoing at the Company; even though Hansen itself had not issued any projections or estimates for its third-quarter results upon which investors could have relied; and even though Hansen – and its shareholders – enjoyed spectacular success during the relevant period. In fact, for 2007 as a whole, Hansen's sales and profits *exceeded* analysts' estimates, and even after the November 2007 drop, Hansen's stock price was *75% above* where it stood at the beginning of the alleged Class Period.[1]

It is axiomatic that a securities class action must be predicated on something more than a drop in the issuer's stock price.[2] Yet it is plain from Plaintiff's shifting theories that there is nothing else behind this suit. The original complaint filed in September 2008 alleged that Hansen and its top officers had committed securities fraud by failing to disclose, *inter alia*, that Hansen's second quarter results were favorably impacted by purchases made by customers in advance of a price increase to take effect the following quarter. Those allegations were frivolous; as the complaint

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[1] Plaintiff purports to bring this action on behalf of all purchasers of Hansen stock between November 9, 2006 and November 8, 2007 (the "Class Period").

[2] *See, e.g.*, H.R. Rep. No. 104-369, at *31 (1995), *reprinted in* 1995 U.S.C.C.A.N. 730 (PSLRA was intended to stop the "routine filing of lawsuits against issuers of securities and others whenever there is a significant change in an issuer's stock price, without regard to any underlying culpability of the issuer, and with only faint hope that the discovery process might lead eventually to some plausible cause of action").

itself showed, Hansen actually disclosed the facts alleged to have been concealed.[3]

The Consolidated Complaint ("Complaint"), filed nearly a year later, abandons these allegations. Plaintiff has now come up with a new theory nowhere mentioned in the original complaint. The Complaint alleges that Hansen made material misrepresentations relating to a distribution arrangement with Anheuser-Busch, Inc. ("AB") and its impact on sales of Hansen's "Allied" energy drink lines, which represent a tiny fraction – a mere 5% – of Hansen's overall sales. But these allegations are just as frivolous as those in the original complaint.

The Complaint does not and cannot allege that Hansen materially misstated *any* financial results or misrepresented *any* material *facts* regarding the AB distribution arrangement or the Allied brands. Rather, the Complaint relies chiefly on allegations that Hansen made general optimistic statements to the effect that it was "happy" with the AB relationship and allegations that Hansen could have done a better job in handling the AB transition and in marketing the Allied products. None of these allegations are even actionable under the federal securities laws, let alone sufficient to satisfy the PSLRA's stringent pleading requirements.

In substance, Plaintiff's claim amounts to this: Hansen's business had some "problems," and therefore when Hansen executives spoke in positive terms about the Company and its prospects, they were committing fraud. As the courts have repeatedly recognized, such a claim is illogical and insufficient under the PSLRA. That is particularly true in this case, given Hansen's performance during the relevant period and the run-of-the-mill nature of the "problems" cited by Plaintiff, which, even as alleged, were extremely minor in the context of the business as a whole.

The Complaint should be dismissed, without leave to replead.

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[3] *Compare* Complaint dated Sept. 11, 2008, ¶¶ 29, 39 (alleging that impact of price increase was not disclosed) *with id.* ¶ 26 (quoting August 2007 earnings call in which Hansen CEO disclosed that price increase "obviously did boost sales a little bit in June [the second quarter], and then it took away from sales in July").

II. STATEMENT OF FACTS

A. Hansen's Business

Hansen, based in Corona, California, is a publicly traded company listed on the NASDAQ stock exchange. (Compl. ¶ 63; Request for Judicial Notice Exhibit ("Ex.") L at 190, 216). Defendant Rodney C. Sacks is Hansen's CEO and Chairman. (Compl. ¶ 56). Defendant Hilton H. Schlosberg is Hansen's Vice Chairman, President, COO and CFO. (Compl. ¶ 57). Defendant Thomas J. Kelly is Vice President of Finance for Hansen Beverage Company ("HBC"), Hansen's chief operating subsidiary. (Compl. ¶ 58). Through HBC and its other subsidiaries, Hansen develops, markets, and sells energy drinks, sodas, juices and other beverages. (Compl. ¶¶ 8, 55).

In 2002, Hansen launched a carbonated energy drink under the Monster Energy brand name ("Monster"), which, as the Complaint notes, was "wildly successful" and by 2006 had become the second most popular energy drink in the country. (Compl. ¶ 12; Ex. C at 10).[4] Monster is part of Hansen's Direct Store Delivery ("DSD") segment. (Compl. ¶ 9; Ex. L at 190). The DSD segment accounts for the vast majority of Hansen's sales and profits: approximately 85-90% of net sales and 97-99% of contribution to operating income during the Class Period. (*See* Exs. L at 229-31, 308; S at 446-48, 491-92). In addition to Monster, the DSD segment includes several other energy drinks, referred to in the Complaint as the "Allied" lines. (Ex. L at 190). The

[4] Plaintiff asserts that prior to Monster's introduction, Hansen was "a mediocre beverage company that struggled to survive" and "even filed for bankruptcy in 1998 because it was apparently unable to pay its payroll taxes." (Compl. ¶ 10). These assertions are not only irrelevant, but completely false and emblematic of the Complaint's pervasive disregard for the facts. From 1996 to 2001, Hansen reported profits each year and its sales nearly tripled. (Exs. A at 3; B at 5). Moreover, Hansen has never filed for bankruptcy. Plaintiff apparently is referring to the bankruptcy filing made in *1988* by another company, Hansen Foods, Inc. (Ex. A at 2), which long preceded Defendants Sacks and Schlosberg's involvement with the Company and Defendant Hansen's ownership of the business, which it acquired in 1992 (Compl. ¶ 11).

Allied brands include Lost Energy Drinks ("Lost"), Rumba Energy Juice ("Rumba"), Unbound Energy Drinks ("Unbound"), Joker Mad Energy Drinks ("Joker") and Ace Energy Drinks ("Ace"). (Compl. ¶ 13; Ex. S at 415).

Although the Complaint repeatedly chastises Hansen for devoting more attention and resources to Monster than to the Allied brands (*see, e.g.*, Compl. ¶¶ 5, 21, 34-38, 105-06), this criticism is perplexing given the relative importance of the different lines to Hansen's business. During the Class Period, Monster was by far Hansen's most important brand, representing approximately 94% of DSD sales (Ex. X at 587) and, therefore, roughly 80-85% of Hansen's overall sales. By contrast, the Allied energy drinks combined represented only 6% of DSD sales and therefore accounted for only about 5% of Hansen's overall sales during the Class Period. In 2006, Monster's share of the market was more than twenty times greater than that of Lost, the largest of the Allied brands. (Ex. W at 560).[5]

As its Monster business grew, Hansen looked for a way to enhance its distribution system, which depended on an amalgam of local, independent beer and liquor distributors and soft-drink bottlers. (Ex. C at 10). In May 2006, Hansen announced that it had reached an agreement with AB, the maker of Budweiser beer, to tap into AB's extensive nationwide network of more than 600 independent distributors (the "AB Distributors"). (Compl. ¶ 15; Exs. C at 10; J at 177, 178). Hansen's subsidiary HBC entered into two long-term "Off-Premise" Distribution Coordination Agreements (the "Off-Premise Agreements") with AB: one for Monster, and one for three of the Allied product lines (Lost, Rumba and Unbound).[6] (Compl. ¶ 15; Ex. L at 223;

[5] The relative importance of these product lines is further demonstrated by the conference call transcripts and analyst reports cited in the Complaint, which reflect minimal discussion of the Allied products and an overwhelming focus on Monster.

[6] "Off-Premise" refers to points of sale where a consumer purchases the beverage and then consumes it off the premises. This category represents the vast majority of the beverage market and includes convenience chains, grocery stores, drug stores, and

Ex. E at 84 (§ 11), 105 (§ 11)). Hansen anticipated that it would transfer about 50% of its distribution to the AB system. (Exs. U at 519; W at 577; X at 599).

Although the Complaint fails to distinguish between AB and the AB Distributors, the agreements assigned different duties to them. Specifically, the Off-Premise Agreements contemplated that the distribution of Hansen products to off-premise channels would be done by the AB Distributors, not by AB. (Ex. E at 76 (Rec. 3), 96 (Rec. 3)). AB's obligations were limited to facilitating and supporting the relationship between Hansen and the AB Distributors. (Ex. E at 76, 78 (§§ 1, 4.1-4.4), 96, 98 (§§ 1, 4.1-4.4)). Although the Off-Premise Agreements gave Hansen access to the hundreds of AB Distributors that comprised AB's distribution network, Hansen had to negotiate and enter into separate distribution agreements with each AB Distributor. (*See* Exs. E at 76-78 (Rec. 3, §§ 1, 2.4, 3), 96-98 (Rec. 3, §§ 1, 2.2, 3); V at 543).

In February 2007, HBC and AB also entered into a separate "On-Premise" Distribution Coordination Agreement (the "On-Premise Agreement") for the Monster brand. (Ex. H at 137). The On-Premise Agreement created a joint venture, whose purpose was to help Hansen get a foothold in bars, nightclubs and other places licensed to sell alcohol for on-premise consumption, which represented a largely untapped but small niche market for the Company. (*Id.* at 137-38). The On-Premise Agreement required AB to assume "primary responsibility for the marketing, promotion, merchandising and sales of [Monster brand products] to On-Premise Accounts only . . . ." (*Id.* at 137, 140 (Rec. 5)).

B. Hansen's Performance

Driven by the phenomenal success of Monster, Hansen has consistently reported record sales and profits over the last several years, including throughout the Class Period. From 2003 to 2007, Hansen's net sales rose from $110 million to more than $904 million. (Ex. S at 438). Net income during that five-year period increased

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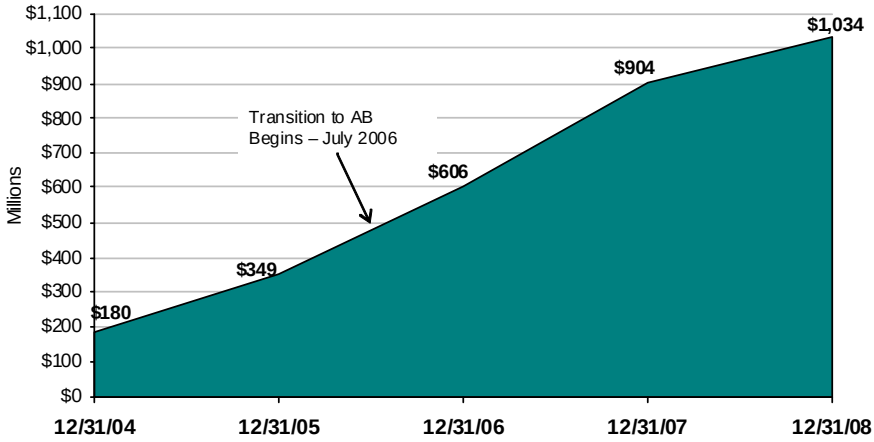
mass merchandisers. (Compl. ¶ 15; *see also* Ex. L at 202).

from $6 million to $149 million. (*Id.*). As a consequence, Hansen's stock price has also grown dramatically, generating enormous benefits for its stockholders. From 2003 to 2007, Hansen's stock price climbed from $0.53 per share to $44.29 on a split-adjusted basis (or from $4.25 per share to $354.32 on a pre-split basis), an increase of more than 8,000%. (Exs. S at 438; JJ at 747, 733).[7]

Hansen's explosive growth continued after it began implementing the AB distribution arrangement in the second half of 2006. Notwithstanding the Complaint's rhetoric about Hansen's "declining," "deteriorat[ing]" or "collaps[ing]" sales (Compl. ¶¶ 18, 26, 102), Hansen posted *record* sales in *each* quarter during the Class Period. Compared to the prior year, Hansen's net sales increased by 38.1% in the first quarter of 2007, by 56.9% in the second quarter, by 38.4% in the third quarter, and by 63.0% in the fourth quarter. (Exs. K at 182; N at 352; Q at 399; R at 407). For the year as a whole, Hansen's net sales grew by nearly $300 million – the largest increase in the Company's history. (Ex. S at 438). As demonstrated by the following chart,[8] the AB relationship was followed not by a decline, but by a huge increase in Hansen's annual net sales:



[7] In fact, Hansen was *the single best* performing stock in the United States during both the 5-year period and the 10-year period ending in 2007. (Ex. II 731-32 (noting that "[a]n investment of $1,000 in Hansen stock at the end of 1997 would have been worth a whopping $195,489 a decade later, compared with $1,776 for a similar investment in the Standard & Poor's 500-stock index")).

[8] (*See* Exs. T at 508; V at 543).

Not only did sales increase under the AB relationship, but so too did Hansen's share of the overall energy drink market. When the AB deal was announced in May 2006, Monster had a 19.4% share of the energy drink market. (Ex. C at 10). At the end of the Class Period – after operating under the AB distribution system – Monster's market share had risen to 24.9%, outperforming its competitors. (Ex. BB at 652). Hansen's profitability also improved. Hansen's net income decreased by 4.2% in the first quarter of 2007, and then rose by 62.7% in the second quarter, by 73.1% in the third quarter, and by 103.1% in the fourth quarter. (Exs. M at 337; N at 352; Q at 399; R at 407). On a year over year basis, net income grew from $98 million in 2006 to $149 million in 2007, an increase of 52.5%. (Ex. S at 445).

Hansen's stock price also continued to climb as the transition to the AB network progressed. When the Class Period began on November 9, 2006, Hansen's shares were trading at $24.88. (Ex. JJ at 746). At the end of the Class Period on November 8, 2007 – *after* the decline following release of the third-quarter 2007 results – Hansen's shares were trading at $43.50. (*Id*. at 734). This represents an appreciation of 74.8% in one year's time and the creation of nearly $1.7 billion in shareholder value.[9]

C. The Allegations of the Complaint

1. The Purported Misrepresentations and Omissions

The Complaint alleges that, from November 2006 to August 2007, Hansen made a series of "false and misleading statements." (Compl. ¶¶ 64-92). Virtually all the purported misrepresentations are alleged to have taken place in quarterly earnings conference calls led by Hansen's CEO, Rodney Sacks.

Notwithstanding the huge improvement in Hansen's sales, profits, and stock price that followed the implementation of the AB agreements, the Complaint's central allegation is that Hansen's top officers committed securities fraud when its CEO

[9] Hansen had roughly 90 million shares outstanding in 2007. (Ex. L at 188).

stated that the transition to the AB distribution system was "progressing well" and that they were "generally very happy" with the AB relationship and viewed it as a "positive" relationship for Hansen. (*See*, *e.g.*, Compl. ¶¶ 2, 4, 72, 77, 85). According to the Complaint, these statements were false and fraudulent because "the [AB] relationship encountered significant problems," including that some AB Distributors allegedly had no interest in distributing Hansen's Allied products and that some AB Distributors were restricted from selling Hansen products because of alcohol regulations. (Compl. ¶¶ 3-4, 81).

Nowhere, however, does the Complaint explain why the existence of isolated problems with the AB transition – which would be expected in any significant business transition – meant that the AB relationship as a whole was not progressing well or having a positive impact on Hansen's distribution and sales. Moreover, as detailed below, the Complaint itself and the conference call transcripts on which it relies show that Hansen specifically and repeatedly disclosed the issues relating to the AB transition throughout the Class Period.

The Complaint also alleges that Hansen made false statements concerning sales of the Allied brands. There is no allegation, however, that Hansen *ever* misrepresented actual sales for the Allied products, and as detailed below, Hansen's CEO candidly disclosed throughout the Class Period that Hansen faced challenges with the Allied products. The purported "false statements" consist of Hansen's CEO expressing, in highly general terms, the hope that sales of Allied products would improve. (Compl. ¶¶ 66, 73). The Complaint is devoid of any facts adequately alleging that these statements were false, much less knowingly false, when made.

Although the Complaint proclaims that Hansen's second-quarter 2007 results were "false," the *sole* basis for this inflammatory charge turns out to be a single vague allegation that a former Hansen employee was instructed to "withhold" some "promotional expenses" estimated to be in the "hundreds of thousands of dollars." (Compl. ¶¶ 6, 89). The Complaint pleads no particularized facts indicating that there

was any violation of accounting rules, let alone fraud; that any of the Defendants had any knowledge whatsoever of any impropriety; or that the amount involved was material to Hansen's financial statements.

The 65-page Complaint cites *not a single* documentary source in support of its sweeping fraud allegations, but instead is replete with conclusory statements that have been purportedly "confirmed" or "reported" by various unnamed former Hansen employees and by one or at most two of the hundreds of AB Distributors. None of these alleged confidential witnesses, however, suggests that any of the Defendants were involved in fraudulent activity.

2. The November 8, 2007 Conference Call

The Complaint further alleges that the "truth" about the AB relationship and sales of Hansen's Allied brands was "reveal[ed]" in Hansen's earnings call for the third quarter of 2007 held on November 8, 2007. (Compl. ¶ 48). In that call, the Complaint alleges, Hansen "admitted that [it] had put the brake on the AB transition." (Compl. ¶ 7). But as the very conference call transcripts cited in the Complaint clearly demonstrate, there was no "admission" at all. In prior conference calls in May and August 2007, Hansen had already announced that the AB transition was "largely done" (Ex. Z at 627) and "largely complete" (Ex. AA at 635). Thus when Sacks reported in the November 2007 call that, "[a]s I've indicated previously, by and large, the transition arrangements to the A-B system is largely complete" (Ex. BB at 653), he was saying nothing different from what he had been saying for months.

Nor was there any "admission" whatsoever in the November 2007 call that the AB system had hurt Hansen's business or that Hansen was no longer happy with it. On the contrary, Sacks expressly noted that "you [can] see from the distribution numbers overall . . . we have increased [our distribution] pretty significantly" as a result of the AB transition, and he reaffirmed that "by and large we are certainly happy. If somebody asked me, looking back, would we have done the A-B transition again? Yes, we would've. Absolutely. We think that was the right [decision] for the com-

pany. . . ." (*Id.*).

The Complaint further alleges that Hansen stated in the November 8 earnings call that its "Allied products had missed internal expectations by $10 million." (Compl. ¶ 7). But this was no acknowledgement of a prior misstatement either, for the Complaint does not and cannot allege that Hansen had made any prior public statement projecting what sales of Allied products would be in the third quarter. Indeed, there is no allegation in the Complaint that Hansen has ever issued financial projections of any kind or given earnings estimates to securities analysts. To the contrary, the Complaint speaks only of estimates or guidance made by *third-party analysts*. (*See, e.g.*, Compl. ¶¶ 6-7, 18, 26, 47-48, 93).

Overall, Hansen again reported record sales and profits for the third quarter of 2007: a 38.4% increase in net sales over the prior year and a 73.1% increase in earnings. (Ex. Q at 399). While this may have fallen short of some analysts' third quarter estimates, Sacks stated that sales in October (the first month of the fourth quarter) had grown by 48%. (Ex. BB at 652). (Ex. BB at 652). When the full-year 2007 results came in a few months later, Hansen's sales and earnings per share had in fact *exceeded* these same analysts' estimates.[10]

3. The Insider Trading Allegations

The Complaint also makes unsubstantiated allegations of "insider trading" against the Individual Defendants, claiming that they "unloaded" Hansen shares between August 13 and September 14, 2007 "to take advantage of material non-public information" prior to the November 2007 price drop. (Compl. ¶¶ 6, 47, 92, 110-14). Far from suggesting fraud, however, these allegations bolster the opposite inference,

[10] *Compare* Exs. FF at 705; GG at 714; HH at 724 (analyst reports issued in August 2007 estimating Hansen 2007 net sales between $863.0 million and $888.1 million and earnings per share (diluted) between $1.46 and $1.48) *with* Ex. S at 445 (reporting Hansen 2007 net sales of $904.5 million and earnings per share (diluted) of $1.51).

i.e., that the Individual Defendants did *not* sell their shares based on inside information.

As the price chart set forth in the Complaint itself shows, the Individual Defendants' sales took place prior to the substantial run-up in Hansen's stock price that preceded the November drop, and at prices that were in the *same range* at which the stock traded *following* the November drop. (Compl. ¶ 110). In fact, most of the Individual Defendants' stock sales were at prices (between $44.01 and $44.14) that were *below* the average price at which Hansen's stock traded from November 8 – when Plaintiff alleges that the "truth" was revealed – through the end of the year ($44.77). (Compl. ¶ 110; Ex. JJ at 733-34).

III. ARGUMENT

A. The Complaint Fails to State a Claim Under Section 10(b) or Rule 10b-5 for Alleged False or Misleading Statements

Plaintiffs in private securities fraud class actions "face formidable pleading requirements to properly state a claim and avoid dismissal under Fed. R. Civ. P. 12(b)(6)." *Metzler Inv. GmbH v. Corinthian Colls., Inc.*, 540 F.3d 1049, 1054-55 (9th Cir. 2008). The elements of a claim for securities fraud under Section 10(b) and Rule 10b-5 are: (1) a material misrepresentation or omission of fact, (2) scienter, (3) a connection with the purchase or sale of a security, (4) transaction and loss causation, and (5) economic loss. *Zucco Partners, LLC v. Digimarc Corp.*, 552 F.3d 981, 990 (9th Cir. 2009).

To withstand a motion to dismiss, the complaint "must satisfy the dual pleading requirements of Federal Rule of Civil Procedure 9(b) and the PSLRA." *Id.* Rule 9(b) provides that "a party must state with particularity the circumstances constituting fraud or mistake." Under Rule 9(b), "[t]he plaintiff must set forth what is false or misleading about a statement" and provide "an explanation as to why the disputed statement was untrue or misleading *when made*." *In re GlenFed, Inc. Sec. Litig.*, 42 F.3d 1541, 1548-49 (9th Cir. 1994) (emphasis in original); *see also Vess v. Ciba-*

Geigy Corp. USA, 317 F.3d 1097, 1106 (9th Cir. 2003) (Rule 9(b) requires averments of "the who, what, when, where, and how of the misconduct charged").

The PSLRA imposes even "more exacting pleading requirements," *Zucco Partners*, 552 F.3d at 990, which serve as a "check against abusive litigation by private parties" in securities fraud cases. *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 313 (2007). The PSLRA requires plaintiffs to "specify each statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed." 15 U.S.C. § 78u-4(b)(1)(B).

"[T]he PSLRA also requires a plaintiff to plead scienter with particularity." *Rubke v. Capitol Bancorp Ltd.*, 551 F.3d 1156, 1164 (9th Cir. 2009). Plaintiffs must "state with particularity facts giving rise to a *strong* inference that the defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2) (emphasis added). A plaintiff must show that the false statement was made intentionally or with a "degree of recklessness that strongly suggests actual intent." *In re Silicon Graphics Sec. Litig.*, 183 F.3d 970, 977-79 (9th Cir 1999); *see also Zucco Partners*, 552 F.3d at 991 (deliberate recklessness standard is "a form of intentional or knowing misconduct"). It is not enough for a complaint "to allege facts from which an inference of scienter rationally *could* be drawn." *Tellabs*, 551 U.S. at 323 (emphasis in original). Rather, the facts alleged, "taken collectively," must give rise to an inference of scienter that is "cogent and at least as compelling as any opposing inference one could draw . . . ." *Id.* at 323-24.

Thus, the PSLRA requires that a securities fraud complaint "plead with particularity both falsity and scienter." *Gompper v. VISX, Inc.*, 298 F.3d 893, 895 (9th Cir. 2002). Because the Complaint here fails to plead either falsity or scienter in conformity with the heightened requirements of the PSLRA and Rule 9(b), it must be dismissed. *See* 15 U.S.C. § 78u-4(b)(3)(A) (mandating that "the court *shall*, on the mo-

tion of any defendant, dismiss the complaint if" these two requirements are not met (emphasis added)).

1. The Complaint Fails to Plead that Defendants Made Any Material Misrepresentations or Omissions About the AB Transition or the Allied Brands

Except for the patently deficient allegations concerning Hansen's purported failure to account for certain "promotional expenses" in the second quarter of 2007, which are addressed below in Point III.A.2., nowhere does Plaintiff allege that any of Hansen's publicly-reported financial information was misstated. Instead, Plaintiff claims that Hansen's CEO Sacks made false or misleading statements about Hansen's transition to the AB distribution system and about the success of the Allied brands during analyst calls and in a single press release.[11]

As discussed below, Plaintiff has failed adequately to plead that any of the statements made by Sacks were false or misleading for the following five independent reasons: (a) the statements at issue are general statements of corporate optimism, which are not actionable as a matter of law; (b) most of the statements constitute forward-looking statements, which are protected by the bespeaks cautions doctrine and the PSLRA; (c) the problems that Plaintiff alleges existed at Hansen do not render any of the statements made by Sacks false or misleading; (d) the issues that Plaintiff claims Sacks concealed were in fact repeatedly disclosed; and (e) allegations of corporate mismanagement do not give rise to a securities fraud claim.

[11] Although Plaintiff names both Sacks and Schlosberg in the first cause of action, the Complaint does not allege that Schlosberg made *any* of the allegedly false or misleading statements. Nor does the Complaint plead particularized facts showing Schlosberg's involvement in preparing, drafting or disseminating *any* of the allegedly false or misleading statements. For this reason alone, the Complaint fails to state a Section 10(b) misrepresentation claim against Schlosberg. *See In re Hansen Natural Corp. Sec. Litig.*, 527 F. Supp. 2d 1142, 1153 (C.D. Cal. 2007).

a. General Statements of Corporate Optimism Are Not Actionable as a Matter of Law

"[V]ague, generalized assertions of corporate optimism or statements of 'mere puffing' are not actionable material misrepresentations under federal securities laws." *In re Impac Mortgage Holdings, Inc. Sec. Litig.*, 554 F. Supp. 2d 1083, 1096 (C.D. Cal. 2008). Such statements "are considered immaterial and discounted by the market" because "reasonable investors do not consider 'soft' statements or loose predictions important in making investment decisions." *In re Leapfrog Enters., Inc. Sec. Litig.*, 527 F. Supp. 2d 1033, 1049 (N.D. Cal. 2007) (citation omitted); *see also In re Gupta Corp. Sec. Litig.*, 900 F. Supp. 1217, 1235 (N.D. Cal. 1994) ("Numerous courts have held . . . that general statements of optimism about the future and 'puffing' about a company or product are not actionable.").

The statements quoted in the Complaint are precisely the kind of indeterminate statements of opinion and optimism that courts routinely conclude are not actionable. For example, with respect to the AB transition, the Complaint alleges that the following statements by Sacks were "false":

- "We *think* that the transition to [AB] is really *going to continue to help us*. . . . We really are very *happy* with the transition." (Compl. ¶ 65).
- "We *look forward* to working together [with AB] to build on the *success* of Monster Energy® and our other energy drink brands." (*Id.* ¶ 70).
- The AB on-premise agreement "*will enable us* to secure quite extensive distribution in the on-premise channel." (*Id.* ¶ 71).
- The AB system "has *improved* the *quality* of our distribution in stores, execution, [and] point of sale merchandising . . . . Generally so, we are *happy* with – with [the AB] system . . . ." (*Id.* ¶ 72).
- "But *going forward*, overall, we're still very *positive* about the relationship and about the *quality* of the distribution and the *long-term strength* that this distribution system will bring to our Company . . . ." (*Id.* ¶ 77).
- "We *think* it is working for us, we're getting good *solid* distribution, we're working with professional distributors, and so we are generally very *happy*." (*Id.* ¶ 85).

- "I *think* the *proof is in the pudding*, it is happening for us and it *will continue to, we think, improve, as we go forward*." (*Id.* ¶ 86) (emphasis added or modified throughout)).

The alleged misrepresentations regarding the Allied brands are of the same kind:

- "[W]e're still very *positive* about Lost. . . . Joker is at a *good velocity* and so is Unbound. . . . We really do *believe* that those products do have *good opportunity*. . . . [W]e do believe Rumba has got *a lot of legs* . . . ." (*Id.* ¶ 65).
- "[W]e're *hoping* that we *will* also be able to offset [any potential decrease in gross margins due to the buy in for 24-ounce Monster cans] by the increased sales in Ace, Joker and Unbound . . . , so we *think* those will also help *improve* our [margins]." (*Id.* ¶ 66).
- "[W]e *think* we'll be able to *improve* our distribution with Lost *as we go forward*." (*Id.* ¶ 73) (emphasis added or modified throughout).

All of these allegations fail as a matter of law. *See, e.g., Impac*, 554 F. Supp. 2d at 1096 (CEO's statements that "[w]e continue to expect solid loan acquisitions and originations" and "[w]e remain optimistic for continued solid loan production" were not actionable); *Leapfrog*, 527 F. Supp. 2d at 1050 ("we feel very positive," "we continue to make strong growth in supply chain" and "[w]e are pleased with our progress" were "soft statements or loose predictions that do not give rise to a securities fraud claim"); *In re Copper Mountain Sec. Litig.*, 311 F. Supp. 2d 857, 868-69 (N.D. Cal. 2004) (statements that business remained "strong," that demand "will continue to grow" and that consolidation in the DSL market would be "very positive" for the company "constitute run-of-the-mill corporate optimism on which no reasonable investor would rely"); *In re Splash Tech. Holdings, Inc. Sec. Litig. ("Splash Tech. II")*, 160 F. Supp. 2d 1059, 1076-77 (N.D. Cal. 2001) (holding that phrases such as "strong," "solid," "improved," and "unfolding as planned" when used to describe demand, results, and growth strategy were not actionable as material misrepresentations); *Grossman v. Novell, Inc.*, 120 F.3d 1112, 1121-22 (10th Cir. 1997) (statements attributing "substantial success" to the integration of sales forces after a merger were

the sort of soft statements that courts routinely dismiss as vague).

b. Forward-Looking Statements Are Protected by the Bespeaks Caution Doctrine and the PSLRA

"'The bespeaks caution doctrine provides a mechanism by which a court can rule as a matter of law . . . that defendants' forward-looking representations contained enough cautionary language or risk disclosure to protect the defendant against claims of securities fraud.'" *Employers Teamsters Local Nos. 175 and 505 Pension Trust Fund v. Clorox Co.*, 353 F.3d 1125, 1132 (9th Cir. 2004) (quoting *In re Worlds of Wonder Sec. Litig.*, 35 F.3d 1407, 1413 (9th Cir. 1994)). The PSLRA's safe harbor is a statutory version of this doctrine. *Id.* It independently protects defendants from liability for a forward-looking statement, provided that the statement is "identified as a forward-looking statement, and is accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward looking statement." 15 U.S.C. § 78u-5(c)(1)(A)(i).[12]

As is clear from the quotations above, the vast majority of the statements by Sacks about Hansen's distribution relationship with AB and the Allied brands were forward-looking statements. The PSLRA defines "forward-looking statement[s]" to include statements regarding "a projection of revenues [or] income," "the plans and objectives of management for future operations," and "future economic performance." 15 U.S.C. § 78u-5(i)(1). In addition, a present-tense statement may qualify as forward-looking if "the truth or falsity of the statement cannot be discerned until

[12] Alternatively, even if a forward-looking statement fails to meet these requirements, it still is protected unless the plaintiff can meet its heavy burden to plead facts to show that the alleged misstatement was made with "actual knowledge" of its falsity. 15 U.S.C. § 78u-5(c)(1)(B); *see also Splash Tech II.*, 160 F. Supp. 2d at 1069 ("Where a plaintiff alleges false forward-looking statements, the 'required state of mind' is 'actual knowledge' that the statement was false at the time it was made." (citation omitted)). As set forth below in Point III.A.3., Plaintiff has failed to plead a strong inference of actual knowledge.

some point in time after the statement is made." *In re Splash Tech. Holdings, Inc. Sec. Litig. ("Splash Tech. I")*, No. C 99-00109, 2000 WL 1727377, at *6 (N.D. Cal. Sept. 29, 2000). Statements that Hansen looks *forward* to working with AB, *expects* distribution to *continue* to improve, and *hopes* that sales of Allied products will improve are forward-looking. *See, e.g.*, *Impac*, 554 F. Supp. 2d at 1098-99 (holding that statements of expected "continued solid loan production" are forward-looking statements); *Leapfrog*, 527 F. Supp. 2d at 1046-47 (holding that statements of "expectations of further improvements in gross margins" are forward-looking statements).[13]

Nor can it be disputed that these statements were identified as forward-looking and accompanied by meaningful cautionary language. Cautionary language is "meaningful" if it "'relate[s] directly to that which plaintiffs claim to have been misled.'" *Leapfrog*, 527 F. Supp. 2d at 1047 (quoting *Worlds of Wonder*, 35 F.3d at 1415).[14] Sacks began each analyst call that is referred to in the Complaint by caution-

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[13] Indeed, Hansen's SEC reports specifically advised investors that "[a]ll statements which address operating performance, events or developments that management expects or anticipates will or may occur in the future including . . . statements expressing general optimism about future operating results and non historical information, are forward looking statements" and that "the words 'believes,' 'thinks,' 'anticipates,' 'plans,' 'expects,' and similar expressions are intended to identify forward-looking statements." (Exs. D at 60; L at 240).

[14] Where, as here (Compl. ¶¶ 124-25), the Complaint relies on the "fraud-on-the-market" presumption, which posits that the market is efficient and promptly digests *all* publicly available information regarding an issuer, "the defendants' cautionary statements must be treated as if attached to every one of its oral and written statements,'" and "the Court must consider whether any cautionary language provided by the defendants *at any time* sufficiently warned of the risk of which plaintiffs complain." *In re eSpeed, Inc. Sec. Litig.*, 457 F. Supp. 2d 266, 280 (S.D.N.Y. 2006) (citation omitted) (emphasis added); *In re Gilat Satellite Networks, Ltd.*, No. CV-02-1510 (CPS), 2005 WL 2277476, at *13 (E.D.N.Y. Sept. 19, 2005); *accord Asher v. Baxter Int'l, Inc.*, 377 F.3d 727, 731-32 (7th Cir. 2004) (oral statements need not include or reference risks where plaintiff relies on fraud-on-the-market theory); *see also Splash Tech. I*, 2000 WL 1727377, at *10 (under bespeaks caution doctrine, oral forward-looking statements must be considered in light of

ing that "certain statements made in [the call] may constitute forward-looking statements" and that "these statements are qualified by their terms or important factors, many of which are outside the control of the Company that could cause actual results and events to differ materially from the statements made [in the call]." (Exs. W at 557-58; *see also* X at 584; Y at 603; AA at 632; BB at 648). The analyst calls were each preceded by a press release cautioning that the Company's forward-looking statements were qualified by the risk factors set forth in the release itself and in Hansen's financial statements. (Exs. G at 130; I at 174; K at 183; N at 353; Q at 401).

Hansen's SEC reports, in turn, detailed a variety of "risks, uncertainties and other factors, that could cause actual results and events to differ materially" from Hansen's statements, and expressly cautioned investors that "[g]iven these uncertainties, you should not rely on forward-looking statements." (*E.g.* Exs. D at 60-61; L at 240, 242; P at 386-88). These included risk factors specifically related to the matters that are the subject of the forward-looking statements challenged in the Complaint. For example, Hansen specifically identified as one risk factor "[t]he marketing efforts of distributors of the Company's products, most of which distribute products that are competitive with the products of the Company." (Exs. D at 61; L at 241; I at 174; K at 183; P at 387). Similarly, Hansen specifically identified risk factors that related to product distribution, including the AB distribution agreements:

> Disruption in distribution or sales and/or decline in sales due to the termination of the distribution agreements with certain of the Company's existing distributors or distribution networks and the appointment of selected AB wholesalers as distributors in their place for the territories of such terminated distributors.

(Exs. D at 61; L at 241; P at 387). Accordingly, Plaintiff cannot state a securities fraud claim based on any of the forward-looking statements set forth in the Com-

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cautionary language in company's SEC filings).

plaint.[15]

c. Allegations of Business Problems Do Not Render Hansen's Statements False

Even if any of the challenged statements were not simply inactionable statements of optimism or forward-looking statements, the Complaint would still be fatally defective because it fails to allege sufficiently that any such statement was false.

Plaintiff alleges that Hansen's positive statements were false and misleading because of various "problems" (*see, e.g.*, Compl. ¶¶ 23, 67, 81) that allegedly plagued its transition to the AB distribution system and sales of the Allied products. These alleged problems included that (i) AB Distributors wanted only Monster and lacked interest in the Allied brands because the brands were not well-known or well-received in the marketplace (Compl. ¶¶ 3, 4, 22, 68, 75); (ii) AB Distributors were restricted from distributing Hansen's products in many areas because of alcohol regulations, in-

[15] Plaintiff also alleges that statements in a May 2007 JP Morgan analyst report were false. (Compl. ¶¶ 79-80). Because Defendants never adopted or endorsed the report, they can be held liable only for their own statements to the analyst. *See In re Syntex Corp. Sec. Litig.*, 95 F.3d 922, 934 (9th Cir. 1996); *In re SeeBeyond Techs. Corp. Sec. Litig.*, 266 F. Supp. 2d 1150, 1170-71 (C.D. Cal. 2003). It is not enough to assert that the report was based on information provided by Sacks and Schlosberg; Plaintiff must identify the specific statements that they made to the analyst and the reasons why the statements were false or misleading when made. *See In re Dura Pharm. Sec. Litig.*, 452 F. Supp. 2d 1005, 1035 (S.D. Cal. 2006); *SeeBeyond*, 266 F. Supp. 2d at 1170. Plaintiff has not done so.

First, neither the Complaint nor the JP Morgan report identifies Sacks' or Schlosberg's specific statements to the analyst. The report merely references "Hansen's commentary" during "a recent positive management meeting with CEO Rodney Sacks and CFO Hilton Schlosberg." (Compl. ¶ 79). Given that the report, at best, paraphrases statements made at the meeting, neither Sacks nor Schlosberg can be held liable for federal securities fraud for the report's statements. *See Leapfrog*, 527 F. Supp. 2d at 1051-52 (rejecting allegations where "analyst 'repackaged' defendants' statements in 'vague and impressionistic terms' rather than the mere reporting of defendants' actual statements"). Second, even if the report's statements could be attributed to Sacks and Schlosberg (which they cannot), the statements still would not be actionable for the reasons discussed herein.

creasing Hansen's costs (*e.g.*, Compl. ¶¶ 4, 30-32, 67); (iii) Hansen was not devoting enough marketing resources to the Allied brands and instead was spending 90% of its marketing budget on Monster (Compl. ¶¶ 5, 34-35, 68, 82, 105); and (iv) certain on-premise markets were difficult to break into due to Red Bull's exclusivity agreements in those markets (Compl. ¶¶ 33, 91). To support these allegations, Plaintiff relies exclusively on the reports of confidential witnesses. However, as explained below in Point III.A.3.b., the Complaint fails to describe its confidential witnesses with sufficient particularity to establish their reliability and personal knowledge, as required by the PSLRA. *See, e.g., Zucco Partners*, 552 F.3d 981 at 995.

But even assuming, *arguendo*, that these various "problems" existed, they in no way establish the falsity of any of the challenged statements. Claims that AB Distributors were most interested in Monster, that some AB Distributors were hindered by alcohol regulations, or that Hansen could have spent more marketing dollars on Allied products simply do not render false Sacks' general positive statements about the AB transition or the prospects for the Allied products. The Courts of this Circuit have recognized time and again that such allegations fail to state a claim for violation of the federal securities laws. As recently stated by one court in words equally applicable to this case:

> Plaintiffs' complaint merely juxtaposes public statements expressing enthusiasm for Yahoo! with paragraphs referring to myriad internal problems at Yahoo!. Alleging a litany of problems is not enough to refute specifically general statements that project optimism and Yahoo!'s growth. As the Court previously noted, in a business as large and complex as Yahoo!, "problems and difficulties are the daily work of business people. That they exist does not make a lie out of any alleged false statement."

Brodsky v. Yahoo! Inc., 630 F. Supp. 2d 1104, 1114 (N.D. Cal. 2009) (quoting *Ronconi v. Larkin*, 253 F.3d 423, 434 (9th Cir. 2001); *accord, e.g., In re Petco Animal Supplies Inc. Sec. Litig.*, No. 05-CV-0823, 2005 WL 5957816, at *20-26 (S.D. Cal. Aug. 1, 2005); *In re Netflix, Inc. Sec. Litig.*, No. C04-2978, 2005 WL 1562858, at *7 (N.D. Cal. June 28, 2005); *Wenger v. Lumisys, Inc.*, 2 F. Supp. 2d 1231, 1247 (N.D.

Cal. 1998) ("All businesses from time to time suffer management problems and product delays, but many manage to 'do very well' despite those commonplace business wobbles.").

This is especially true here. It is undisputed that Hansen reported substantial *increases* in sales and profits throughout the Class Period (and beyond), following implementation of the AB agreements. Hansen's transition to the AB network was a nationwide effort involving hundreds of AB Distributors and primarily directed at improving distribution levels and sales of Monster, Hansen's flagship brand. In this light, the Complaint's allegations of peripheral problems predominately affecting a few AB Distributors and the Allied brands – which comprised only 5% of Hansen's overall sales – are patently insufficient to establish that Hansen's positive statements about the AB system were false.[16] *See Petco*, 2005 WL 5957816, at *23 (alleged operational problems did not render false company's statements given that it had a successful business strategy given, *inter alia*, its sales growth and earnings record during the class period).

Similarly, the Complaint fails to explain how the alleged problems rendered false Sacks' hopeful statements regarding the Allied brands. There is no allegation in the Complaint that Hansen's internal projections for Allied products were inconsistent with Sacks' statements. On the contrary, the Complaint affirmatively alleges that Hansen's internal projections assumed an *increase* in Allied sales. (*See* Compl. ¶ 7). Alleged problems with the marketing of Allied products in no way establish that Sacks' statements were false. *See Ronconi*, 253 F.3d at 434 ("A company could experience 'serious operational problems,' 'substantial difficult[ies],' and 'difficult problems' and still have increasing revenue.").

[16] Notably, the Complaint's confidential witnesses do not attempt to describe what impact the supposed issues with the AB transition and the Allied brands had on Hansen's overall business or assert (let alone show) that the impact was material.

d. The Challenges Relating to the AB Transition and the Allied Products Were Expressly Disclosed by Hansen

To state the obvious, where the information alleged by the Complaint to have been omitted was actually disclosed, there can be no basis for a claim of misrepresentation under the federal securities laws. *See, e.g.*, *Belodoff v. Netlist, Inc.*, No. SA CV 07-00677, 2008 WL 2356699, at *9 (S.D. Cal. May 30, 2008). Yet the conference call transcripts cited in the Complaint itself show that Sacks repeatedly disclosed the challenges that Hansen faced with the AB transition and Allied sales, including the very issues the Complaint alleges were concealed from investors.

Plaintiff attempts to avoid acknowledging these disclosures by quoting the transcripts selectively. The full transcripts confirm that, throughout the Class Period, Sacks discussed the issues arising from the transition to the AB distribution system:

- "Rome wasn't built in a day. It takes time. In some of these cases . . . a lot of the distributors haven't [gone through][17] distributing non-alcoholic products. There is a learning curve." (Ex. W at 561).
- "It's taking time in many cases to, you know, change the mind set of the distributors and of their salespeople as to how to sell and how to merchandise energy drinks . . . ." (Ex. X at 592).
- "There are markets where we were weak . . . . [In s]ome of the markets in the Northwest . . . we're not seeing the growth we would have liked to have seen." (Ex. Y at 608).
- "[T]hese [things] do take time. In some markets we have disappointments . . . ." (Ex. AA at 640).

Sacks specifically discussed that some AB Distributors were interested in distributing Monster, and not the Allied brands:

[17] For the Court's convenience, we have made minor modifications based on the audio record to some of the quotations from the investor call transcripts to correct obvious transcription errors. The modifications appear in brackets and have been added solely to make the text more comprehensible; none of the bracketed language materially alters the overall meaning of the quoted language.

- "There were longer negotiations with some of the [AB] distributors who weren't getting Monster, who . . . indicated . . . that [they don't] want to take the other brands, unless they got Monster . . . [and that] [t]here have been some markets that have not agreed to take the brands unless they get Monster . . . ." (Ex. W at 563-64).

- "[W]e did get some resistance" from the AB distributors who "weren't awarded Monster" and who "held out for Monster. . . ." (Ex. X at 594).

- "[A]ll of the Budweiser distributors will be getting the on-premise Monster, and we think that by getting them with the on-premise Monster, . . . those that sort of haven't taken Lost will take Lost, and so, we think we'll be able to improve our distribution with Lost as we go forward. . . ." (*Id.*).

Sacks also specifically discussed that some AB Distributors did not sell in markets due to alcohol regulations, and that AB's on-premise distribution would be adversely affected by competitors' existing agreements:

- "[T]here are some states that . . . whether it is for dry areas or just different channels where they don't permit alcoholic drinks to be sold, and the result is that AB doesn't ordinarily go into it. . . . [T]here may be a little bit of fall off that we'll get. We won't be able to reach as many accounts . . . ." (Ex. W at 577).

- "Until now, as you know, we obviously, attacked that [on-premise] channel, but it has been very difficult. That channel is dominated by Red Bull. They have dominated that channel for over 10 years, and really no one-- none of the competitors have managed to make any inroads into their channel." (Ex. X at 589).

- On-premise establishments have "many existing agreements with competing brands and competing beverages that encompass energy drinks even though they might not be selling them" and that Hansen would have to "wait for the contract[s] to expire . . . ." (Ex. AA at 635).

Likewise, Hansen specifically and repeatedly disclosed that the AB transition had adversely affected sales of Allied products, particularly Lost:

- "So [certainly] Lost-- we think has got hurt this period. We also weren't really able to get started with Rumba. We think the other sort of-- just because of how much work and focus we have got in dealing with A-B and Monster . . . ." (Ex. V at 554).

- "Lost is down from 1.3 to 1.1 [percent] largely [due] to the effects of the transition [that] has been a little bit disruptive to the Lost brand, but it is getting back on stream"; the transition of Lost has been "a struggle." (Ex. W at 560, 563).
- "By and large [the transition] has worked out, but it did take some time and there was disruption. We need to get through it on the Lost brand." (*Id.* at 564).
- "Lost energy lost some ground due to the transition. We are still trying to get the brand back on track and that is taking some effort." (Ex. Y at 606).
- Lost "has sort of struggled a little more. . . . [W]e had lost distribution because of the change-over hadn't gone as smoothly as planned with Lost, and it has been more of a challenge. . . . [I]t has been disappointing that [Lost] has sort of dropped off as it has in the period. . . . [It] is probably about 2 million in sales during the period, less than last year." (*Id.* at 615).

The above disclosures refute any claim that Sacks concealed the alleged problems arising from the transition to the AB distribution system and sales of the Allied brands.[18]

e. Plaintiff's Allegations of Corporate Mismanagement Do Not State a Claim for Securities Fraud

At its core, the Complaint does not rest on any colorable claim of fraudulent conduct, but rather attacks the wisdom of Hansen's sales and marketing strategy. According to Plaintiff, it was a poor business decision for Hansen to enter into the distribution agreements with AB and to allocate more resources to its flagship brand, Monster, than to the Allied products. The Complaint is chock full of such criticisms. (*See, e.g.*, Compl. ¶¶ 33-34, 37, 39, 105).

Plaintiff's questioning of Hansen's business acumen is seriously misguided (especially given Hansen's performance during the Class Period). For example, while the Complaint repeatedly faults Hansen for devoting 90% of its marketing

[18] In addition to Hansen's own disclosures, the securities analysts who tracked Hansen's stock, relying on monthly AC Nielsen sales data, provided investors with their own independent assessments of the impact of the AB transition, noting negatives as well as positives. (*See* Exs. CC at 671; DD at 687, 690; EE at 696, 699).

budget to Monster and only 10% to the Allied brands and other products, this allocation hardly seems unreasonable given that Monster was by far the Company's leading product and accounted for more than 80-85% of its revenues during the Class Period (compared to only 5% for the Allied brands).

But more fundamentally, such allegations simply are not the stuff of a claim for federal securities fraud. The Supreme Court long ago held that allegations of corporate mismanagement do not constitute "manipulative or deceptive" conduct and are not actionable under Section 10(b). *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 471, 479 (1977). It is equally well-settled that such a claim may not be bootstrapped into a cause of action under Section 10(b) by alleging that the mismanagement was not properly disclosed. *See, e.g., Panter v. Marshall Field & Co.*, 646 F.2d 271, 288 (7th Cir. 1981). Courts in this Circuit therefore have repeatedly dismissed such mismanagement claims as not actionable. *See, e.g., Impac*, 554 F. Supp. 2d at 1094-96 (allegations by confidential witnesses of poor judgment and even incompetence "do not show any deceit on the part of Defendants" and therefore "cannot support a fraud claim"); *Petco*, 2005 WL 5957816, at *22 ("Generic allegations of mismanagement could be made against any business, and do not support a federal securities fraud lawsuit."). The same conclusion is compelled here.

2. The Complaint Fails to Plead that Hansen's Quarterly Results Were Materially False

Plaintiff's lone allegation of accounting fraud – relating to Hansen's financial statements for the second quarter of 2007 – also fails to establish the existence of any material misrepresentation. Based on the account of a single confidential witness, "a National Account Manager," Plaintiff alleges that Hansen's "results" for its second quarter of 2007 were false because one of Hansen's vice presidents, who is not a defendant in this action, instructed the witness to "withhold promotional expenses" for one particular account. (Compl. ¶¶ 46, 89). Consequently, "Hansen's 2Q07 financial results . . . did not include what the witness estimated were hundreds of thousands of

dollars of expenses . . . ." (Compl. ¶ 89). These vague and conclusory allegations of accounting fraud do not remotely satisfy the particularity requirements of the PSLRA and Rule 9(b).

"To properly state a claim for accounting fraud, plaintiffs must 'plead facts' sufficient to support a conclusion that [d]efendant [ ] prepared fraudulent financial statements and that the alleged financial fraud was material." *In re Daou Sys., Inc., Sec. Litig.*, 411 F.3d 1006, 1016 (9th Cir. 2005) (citation omitted) (alterations in original). "[T]he complaint *must describe the violations with sufficient particularity*; a general allegation that the practices at issue resulted in a false report of company earnings is not a sufficiently particular claim of misrepresentation." *Id.* (internal quotation marks and citations omitted) (emphasis added). No such particularized facts are pled here.

For starters, Plaintiff fails to describe the confidential witness with sufficient particularity to establish the witness's reliability and personal knowledge, as required by the PSLRA. *See Zucco Partners*, 552 F.3d at 995. There are no particularized facts showing that Plaintiff's confidential witness had any role in Hansen's accounting process or financial reporting. *Brodsky*, 630 F. Supp. 2d at 1114 (for accounting fraud allegation to survive pleading stage, plaintiff "must describe with particularity these CWs' roles in [the company's] revenue recognition process and that they had personal knowledge of Defendants' accounting decisions").

Moreover, the Complaint pleads no facts indicating that any misstatement resulted from the alleged "withholding" of promotional expenses. Plaintiff provides no specifics whatsoever regarding what promotions were involved, when they took place, how the expenses associated with them were "withheld," from whom they were "withheld" or even what is meant by that cryptic word. *See In re Bus. Objects S.A. Sec. Litig.*, No. C 04-2401, 2005 WL 1787860, at *7 (N.D. Cal. July 27, 2005) (rejecting "vague and conclusory" allegation based on confidential witness statement that "some sales were not recorded in the quarter in which they were made;" "[t]he

Court is left to speculate as to the date, sales[,] quantity, and other relevant details regarding the transaction"). Indeed, the Complaint does *not* specifically allege that the promotional expenses were actually incurred in, or required under applicable accounting rules to be accounted for in, the second quarter of 2007, or that they were not actually accounted for in the second quarter.[19]

Finally, the Complaint provides no particulars regarding the impact of the alleged conduct on Hansen's financial statements, *i.e.*, the approximate amount by which a specific line item was overstated. The witness' vague "estimate" that the promotional expenses at issue were in the "hundreds of thousands of dollars" is plainly insufficient. *See In re Vantive Corp. Sec. Litig.*, 283 F.3d 1079, 1090-91 (9th Cir. 2002) (allegations of improper revenue recognition of "millions of dollars" insufficient to plead the amount of the overstatement). Tellingly, the Complaint does not even allege that the purported omission of these promotional expenses had a *material* impact on Hansen's financials – nor could it, given that Hansen reported total net sales of $244.8 million in the second quarter and operating income of $61.4 million. (Ex. P at 379). A few hundred thousand dollars of promotional costs could not have made any conceivable difference to a reasonable investor. *See, e.g., In re Westinghouse Sec. Litig.*, 90 F.3d 696, 714-15 (3d Cir. 1995).

3. The Complaint Fails to Plead Facts Giving Rise to a Strong Inference of Scienter

Even if the Complaint did sufficiently allege a material misrepresentation or omission by any of the Defendants – and it does not – the Complaint would still have to be dismissed because it fails to plead the requisite "strong inference" of scienter.

[19] More specifically, there are no allegations as to what accounting rules applied to the promotional expenses, in what period the expenses were supposed to be recorded, whether the expenses were required to be accrued for in advance, or whether and how Hansen failed properly to accrue for them or to adhere to generally accepted accounting principles in any respect.

The Complaint's scienter allegations, whether examined individually or collectively, fail to give rise to a cogent and compelling inference that Defendants intended to deceive investors, as required by *Tellabs*. *See Zucco Partners*, 552 F.3d at 992 (complaint's scienter allegations should first be examined individually and then holistically to determine if *Tellabs* standard is satisfied).

The most direct way to show that "the party making the statement knew that it was false is via contemporaneous reports of data, available to the party, which contradict the statement." *Nursing Home Pension Fund, Local 144 v. Oracle Corp.*, 380 F.3d 1226, 1230 (9th Cir. 2004); *see also Yourish v. Cal. Amplifier*, 191 F.3d 983, 993 (9th Cir. 1999) (plaintiff must point "to inconsistent contemporaneous statements or information (such as internal reports) which were made by or available to the defendants"). Here, the Complaint cites *no* contemporaneous documents or data suggesting that *any* of the Defendants knew that *any* of the alleged misstatements were false when made.

Instead, the Complaint tries several other tacks, none of which support any inference of scienter – much less a "strong inference" or the "cogent and compelling" inference required by *Tellabs*. First, Plaintiff makes boilerplate allegations about the Individual Defendants' positions as Hansen officers, their access to or receipt of unidentified "information," "specific reports," and "regular briefing[s]," and their signatures on Sarbanes-Oxley certifications. (Compl. ¶¶ 99, 101). Second, Plaintiff relies on amorphous observations of unnamed confidential witnesses, who themselves never suggest that any fraud was afoot. Third, Plaintiff points to the Individual Defendants' stock trades during the class period in an attempt to support its other, factually devoid allegations of scienter. As discussed in more detail below, whether viewed in isolation or holistically, none of these allegations are sufficient to satisfy the pleading standards articulated in *Tellabs* and *Zucco Partners*.

a. Plaintiff's Boilerplate Allegations of Corporate Positions, Access to Information, and Sarbanes-Oxley Certifications Do Not Support an Inference of Scienter

Under the heading "Scienter Allegations," Plaintiff sets forth various boilerplate allegations, including that the "defendants," by virtue of their corporate positions, were aware of the allegedly undisclosed information. (*See* Compl. ¶¶ 97-101). Fraud, however, is not a status offense, and courts have routinely rejected attempts to plead scienter on this basis. *See, e.g.*, *In re U.S. Aggregates, Inc. Sec. Litig.*, 235 F. Supp. 2d 1063, 1074 (N.D. Cal. 2002); *Hansen*, 527 F. Supp. 2d at 1158-59. A ruling to the contrary "would eliminate the necessity for specially pleading scienter, as any corporate officer could be said to possess the requisite knowledge by virtue of his or her position." *In re Audodesk, Inc. Sec. Litig.*, 132 F. Supp. 2d 833, 844 (N.D. Cal. 2000).

Similarly, Plaintiff alleges that the "defendants" should have been aware of the alleged issues by virtue of their access to general company information, attendance at unspecified meetings, participation on equally vague "monthly conference calls," and review of unidentified reports and other data. (Compl. ¶¶ 97, 102). Boilerplate allegations, such as these, are repeatedly and roundly rejected by courts. *See Vantive*, 283 F.3d at 1087 (general allegations of defendants' "hands-on" management style, their interaction with other officers and employees, their attendance at meetings, and their receipt of unspecified weekly or monthly reports are insufficient); *Impac*, 554 F. Supp. 2d at 1100 ("Vague references to 'packages' and 'reports' are the type of boilerplate allegations that courts generally reject as evidence of scienter."); *In re Lockheed Martin Corp. Sec. Litig.*, 272 F. Supp. 2d 944, 956 (C.D. Cal. 2003) (allegations that defendant "received regular updates regarding the status of the Company's major projects" insufficient to allege scienter).

Equally unavailing are Plaintiff's allegations about "binders" of publicly-available "Nielson numbers," and access to sales data in "a computer system called Mass 500" and in "a master spreadsheet." (Compl. ¶¶ 101-102). Under controlling

law in this Circuit, Plaintiff must allege more than the existence of internal reports and data that might have contradicted the information provided to the public; Plaintiff must allege specific facts about the contents of those reports, which officers reviewed them and when, and why the reports were reliable. *In re Blue Rhino Corp. Sec. Litig.*, No. CV 03-3495, 2004 WL 5681763, at *6 (C.D. Cal. Oct. 7, 2004) ("[C]omplaint must 'state facts relating to internal reports, including their contents, who prepared them, which officers reviewed them and from whom [plaintiff] obtained the information.'" (quoting *Silicon Graphics*, 183 F.3d at 984)); *see Metzler*, 540 F.3d at 1066 (mere existence of "sophisticated information management system" insufficient to establish scienter). Here, Plaintiff has pled no such facts.

Nor does the fact that Sacks signed Sarbanes-Oxley certifications support an inference of scienter, as Plaintiff argues. (Compl. ¶ 108). "[R]equired certifications under Sarbanes-Oxley section 302(a) . . . add nothing substantial to the scienter calculus." *Zucco Partners*, 552 F.3d at 1003-04; *see also Glazer Capital Mgmt., LP v. Magistri*, 549 F.3d 736, 747 (9th Cir. 2008) ("Sarbanes-Oxley certifications are not sufficient, without more, to raise a strong inference of scienter").

b. Plaintiff's Confidential Witnesses Do Not Support an Inference of Scienter

Statements from confidential witnesses must pass two "hurdles" to satisfy the PSLRA's pleading requirements. *Zucco Partners*, 552 F.3d at 995. First, the witnesses "must be described with sufficient particularity to establish their reliability and personal knowledge. . . . Second, those statements which are reported by confidential witnesses . . . must themselves be indicative of scienter." *Id.* (citations omitted). The Complaint does not satisfy either requirement.

(i) Plaintiff Fails to Establish the Reliability and Personal Knowledge of the Confidential Witnesses

Where, as here, a complaint lacks documentary evidence, "confidential witness statements may only be relied upon where the confidential witnesses are described 'with sufficient particularity to support the probability that a person in the position

occupied by the source would possess the information alleged.'" *Id.* (citation omitted); *see also Limantour v. Cray Inc.*, 432 F. Supp. 2d 1129, 1142 (W.D. Wash. 2006) (courts should examine, among other things, whether each witness is provided with a number, job title, time period of employment, work location, and a brief job description). The Complaint fails to provide these particulars.

To begin with, none of the witnesses are numbered, making it impossible even to know how many confidential witnesses the Complaint relies on. While the Complaint provides job titles and locations for some witnesses (but not for others), it is clear that in some instances the Complaint refers to multiple witnesses in the same location and with the same title. (*E.g.*, Compl. ¶¶ 32, 35). On a number of occasions the Complaint does not even do that much, resorting instead to reports supposedly from "many AB distributors and Hansen former employees," "numerous former employees," and "countless witnesses." (*E.g.*, Compl. ¶¶ 22, 34, 68, 81). Without a name, number or some other identifying information, there is no way to ascertain which of the Complaint's innumerable witnesses is speaking, and thus no way to measure the credibility and reliability of the speaker.

In addition, the Complaint does not explain the responsibilities or duties of the confidential witnesses. Absent this information, it cannot be determined whether the witnesses would have possessed any of the information ascribed to them.[20] *See*, *e.g.*,

[20] For example, the Complaint leaves unexplained how a low or mid-level "Regional Sales Manager in Texas" would know about "the most significant disagreement between Hansen and AB," how the same or similarly situated sales person in Texas became aware that the entire "Company began shifting a significant amount of its marketing budget to the Monster line," or how a sales person in Arizona learned about the purchasing patterns of consumers in "Kansas, Iowa and elsewhere." (Compl. ¶¶ 17, 34, 39). It is similarly unclear as to what aspects of a "Senior Marketing Manager['s]" undefined duties would have made him or her familiar with "AB's hope of breaking into the on-premise market," its business relationships with restaurants and stores, and the increasing segmentation by bars and restaurants of their distributors. (Compl. ¶ 33). The PSLRA demands more than speculation about

In re Northpoint Comm'ns. Group, Inc. Sec. Litig., 184 F. Supp. 2d 991, 1000 (N.D. Cal. 2001) (finding confidential witness statements insufficient where witness descriptions did not provide their job duties or describe how the witness learned of the information alleged); *In re Tibco Software, Inc.*, No. C 05-2146, 2006 WL 1469654, at *22 (N.D. Cal. May 25, 2006) (finding inadequate job descriptions that did not indicate specific knowledge of the acquisition and forecasting process at issue).

The Complaint likewise fails to allege when any of the witnesses worked for Hansen or AB. Confidential witnesses who were not employed during the events to which their observations and statements relate cannot be given any weight. *See, e.g.*, *Zucco Partners*, 552 F.3d at 996 (complaint failed to plead facts showing the witnesses had personal knowledge of the information alleged, in part because two of the witnesses were not employed when the relevant facts occurred).

Finally, the Complaint improperly attempts to establish the existence of *companywide* problems relating to the AB transition and Allied sales by relying on information allegedly received from confidential witnesses servicing parts of a handful of states (at most six). Allegations that attempt to extrapolate a confidential witness' knowledge of Hansen's business in discrete regional areas to the Company as a whole are insufficiently particular to survive a motion to dismiss. *See Cal. Pub. Employees Ret. Sys. v. Chubb Corp.*, 394 F.3d 126, 148-49 (3d Cir. 2004) (PSLRA not satisfied where plaintiff "heavily rel[ies] on former [local branch office] employees . . . for information concerning the [defendant's] business on a national scale," and does not allege "how or why such [low level, locally sited former employees] would have knowledge that expanded beyond" their area of employment); *In re Zumiez Inc. Sec. Litig.*, No. C07-1980, 2009 WL 901934, at *7 (W.D. Wash. Mar. 30, 2009) (rejecting scienter allegations where confidential witnesses "were in no position to have infor-

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what a witness might have known based on his or her title alone. *See Bus. Objects*, 2005 WL 1787860, at *6.

mation concerning company-wide performance").

(ii) The Confidential Witness Statements Are Not Indicative of Scienter

Even if the Complaint had sufficiently alleged the reliability and personal knowledge of its confidential witnesses (which it has not), the statements that the Complaint attributes to those witnesses are not "indicative of scienter." *Zucco Partners*, 552 F.3d at 995.[21]

Here, no confidential witness provides *any* particularized facts showing that any defendant intentionally or with deliberate recklessness made a false statement or engaged in any other fraud. Indeed, for the most part, Plaintiff simply offers the nebulous opinions of confidential witnesses conveying run-of-the-mill business problems or their disagreement with management's decisions.[22] Not one of the Com-

[21] As the Fifth and Seventh Circuits have explained, allegations based on unnamed witnesses should be steeply discounted in light of the Supreme Court's decision in *Tellabs*. *Higginbotham v. Baxter Int'l Inc.*, 495 F.3d 753, 756-57 (7th Cir. 2007); *Ind. Elec. Workers' Pension Trust Fund IBEW v. Shaw Group, Inc.*, 537 F.3d 527, 535 (5th Cir. 2008); *see also Zucco Partners*, 552 F.3d at 995 n.2. This is because "anonymity conceals information that is essential to the sort of comparative evaluation required by *Tellabs*." *Higginbotham*, 493 F.3d at 757. "It is hard to see how information from anonymous sources could be deemed 'compelling' or how we could take account of plausible opposing inferences. Perhaps these confidential sources have axes to grind. Perhaps they are lying. Perhaps they don't even exist." *Id.*

[22] By way of example, witnesses purportedly "confirmed" or "reported" that Hansen's "marketing plans . . . were *not working*," that "it was *hard* for AB/Hansen to 'get its foot in the door'" with on-premise retailers, that Hansen "began shifting a *significant amount* of its marketing budget to the Monster line," that "Hansen *effectively sacrificed* Allied for Monster success," that "based on interactions with Hansen personnel, the emphasis on Monster produced an *obvious negative effect* on the sales of non-Monster products," that the "Rumba line *suffered* the *same fate* [as Lost] as the Company *struggled* to determine whether to market it as an energy drink," that "the Allied beverages could not *gain traction* because Hansen did not provide *adequate* promotional support when they were launched," and that sales declined "*because Hansen sold [Lost] in states with no relation to surfing*. . . . Lost

plaint's confidential witnesses is reported to have said that any of the Defendants engaged in fraudulent conduct, nor does any witness even assert that any of the statements allegedly made by the Defendants were false. *See Weiss v. Amkor Tech., Inc.*, 527 F. Supp. 2d 938, 955-56 (D. Ariz. 2007) (dismissing complaint with prejudice and noting that "there is no allegation by any [confidential witness] directly asserting that the statements at issue were false").

The statements that are attributed to the confidential witnesses do not support any inference, let alone a strong inference, that any of the Defendants made an intentionally false statement. Thus, for example, confidential witness statements that some AB Distributors were interested only in Monster, that alcohol regulations restricted AB Distributors in certain areas, and that certain on-premise markets had exclusivity agreements with Red Bull (*see, e.g.*, Compl. ¶¶ 21-22, 30-31, 33) do not show that Sacks, contrary to what he stated on analyst calls, in fact was not generally happy with the AB transition or did not think the AB system would improve Hansen's distribution. Not a single confidential witness states that Sacks thought or felt differently about the AB relationship from what he stated on the analyst calls, nor does the Complaint allege that any witness even was in a position to know such information.

Similarly, confidential witness statements that the Company's primary focus was on marketing Monster, that some AB Distributors were not interested in distributing the Allied brands, and that, in the summer of 2007, Sacks emphasized Allied brand sales at a national meeting, made bonuses of sales personnel dependent thereon, and offered promotions on Allied brands (*see, e.g.*, Compl. ¶¶ 34-43) do not show that Sacks – contrary to his statements – was not hopeful about the Allied brands or did not think the AB distribution system would help improve Allied brand distribution. Again, not a single confidential witness states that Sacks thought or felt

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only did well in coastal locations . . . ." (Compl. ¶¶ 33-37, 39) (emphasis added). These are opinions and conclusions, not facts.

differently about the Allied brands from what he stated on the analyst calls, nor does the Complaint allege that any witness was in a position to know such information.

Likewise, no confidential witness states that any Defendant had any awareness that an account manager was purportedly instructed by her supervisor to "withhold reporting promotional costs" in the second quarter of 2007 (Compl. ¶ 89). Rather, a former "Cost Accountant" states only that Kelly was "very diligent" about reviewing Hansen's financial information and that Kelly received reports about Hansen's "poor internal controls." (*Id.* ¶ 109). An allegation that an employee thought Kelly to be very diligent about reviewing financial information and received reports about the Company's controls does not show that Kelly had any knowledge about the alleged withholding of promotional expenses.[23] *See In re Hypercom Corp. Sec. Litig.*, No. CV-05-0455, 2006 WL 1836181, at *6 (D. Ariz. July 5, 2006) (rejecting allegations that defendants must have known about the accounting issues given how "detail-oriented they were").

c. Plaintiff's "Insider Trading" Allegations Do Not Support an Inference of Scienter

Finally, Plaintiff argues that the Individual Defendants' stock sales during the Class Period support an inference of scienter. (Compl. ¶¶ 110-14). For stock sales by corporate insiders to evidence scienter, a plaintiff must plead particularized facts showing that the sales were "unusual" or "suspicious." *See Ronconi*, 253 F.3d at 435. "[I]nsider trading is suspicious only when it is 'dramatically out of line with prior

[23] Similarly unavailing is the Complaint's allegation that "the individual responsible for Sarbanes-Oxley compliance," who is not otherwise identified and is not alleged to be one of the Complaint's witnesses, "would tell Kelly once a month about the discrepancies between the Company's purchase orders and invoices, but Kelly *apparently* did not correct the problem." (Compl. ¶ 109) (emphasis added). This allegation has nothing to do with the alleged false statements in the Complaint, and appears to be based on nothing more than conjecture and impermissible hearsay. *See, e.g., Zucco Partners*, 552 F.3d at 998 n.4 (cautioning against reliance on hearsay statements by confidential witnesses).

trading practices *at times calculated to maximize the personal benefit from undisclosed inside information.'"* *Id.* (quoting *Silicon Graphics*, 183 F.3d at 986) (emphasis added in *Ronconi*). Three factors are used in making this determination: (1) the amount and percentage of shares sold by insiders; (2) the timing of the sales; and (3) whether the sales were consistent with the insider's prior trading history. *Id.* All three factors demonstrate that there was nothing unusual or suspicious about the Individual Defendants' stock sales during the Class Period.

(i) There Is Nothing Suspicious About the Percentages of Shares Sold by Defendants

In computing percentages for insider stock holdings and sales, courts include "'[a]ctual stock shares plus exercisable stock options.'" *Vantive*, 283 F.3d at 1092 n.12 (quoting *Silicon Graphics*, 183 F.3d at 986-87). Accordingly, only the last two columns of the Complaint's stock charts, which represent the Individual Defendants' stock plus vested stock options, are relevant. (Compl. ¶¶ 110, 112). Plaintiff's allegation that Sacks and Schlosberg each sold about 65% of their "Stock Holdings" (*Id.* ¶ 110) is misleading because it excludes their vested options, which represent the vast majority of their holdings. Similarly misleading is the fact that Plaintiff segregates the shares that Sacks and Schlosberg held individually from those they held jointly through various of their entities such as Hilrod Holdings L.P. ("Hilrod I").[24] (*See id.*).

Taking into account the vested options and the shares held through their entities during the Class Period, Sacks sold 13.15% of his total holdings and Schlosberg sold 13.86% of his total holdings.[25] These percentages are not unusual or suspicious.

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[24] In addition to Hilrod I, other entities through which Sacks and Schlosberg held shares during the Class Period include Hilrod Holdings II L.P. ("Hilrod II"), HRS Holdings L.P. ("HRS") (which actually made the sale on August 22, 2007 attributed to Hilrod I in the Complaint), and the Rodney C. Sacks 2007 Grantor Retained Annuity Trust ("RCS 2007 GRAT"). (Exs. KK at 752-64; LL at 768-80).

[25] As alleged in the Complaint, Sacks and Schlosberg each sold 791,500 shares during the Class Period (attributing to each of them 50% of the shares sold by their jointly

See Vantive, 283 F.3d at 1094 (sales by insider of 13% were not suspicious); *Metzler*, 540 F.3d at 1067 (sales of 37% of stock holdings did not support an inference of scienter because the Ninth Circuit "typically require[s] larger sales amounts"); *In re Hienergy Tech., Inc.*, No. SACV04-1226, 2005 WL 3071250, at *7 (C.D. Cal. Oct. 25, 2005) (sales of 20% of insider's holdings were not suspicious enough to support finding of scienter). Indeed, the fact that Sacks and Schlosberg retained over 85% of their holdings actually *negates* any inference of scienter. *Vantive*, 283 F.3d at 1094; *see also In re Apple Computer Sec. Litig.*, 886 F.2d 1109, 1117-18 (9th Cir. 1989) (holding that, despite sales of $84 million in shares, the defendants retained a large percentage of their holdings such that an inference of scienter was negated).[26]

The Complaint alleges that Kelly sold 50.34% of his holding during the Class Period. (Compl. ¶ 110). In fact, Kelly sold 77.32% of his holdings during the Class Period.[27] This circumstance, however, does not support an inference of scienter given that there was nothing suspicious about the sales' timing and the sales were consistent with Kelly's trading history, as explained below. *See Vantive*, 283 F.3d at 1093-94 (insider's sales of 74% of holdings did not raise suspicion to support finding of scienter where sales were not suspicious in their timing and not inconsistent with trading

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held entities). (Compl. ¶ 110; Exs. KK at 752-64; LL at 768-80). Following the last of these sales on September 14, 2007, Sacks had remaining a total of 5,228,500 shares (including 2,159,724 shares and vested options held directly and 3,068,776 shares held through Hilrod I, Hilrod II, HRS and the RCS 2007 GRAT) (Ex. KK at 762-64), and Schlosberg had remaining a total of 4,917,276 shares (including 2,148,500 shares and vested options held directly and 2,768,776 shares held through Hilrod I, Hilrod II and HRS) (Ex. LL at 778-80).

[26] Even if the Complaint's percentages of stock and vested options are used, there is still nothing suspicious. The Complaint alleges that, during the Class Period, Sacks and Schlosberg sold 15.35% and 15.41% of their holdings (including vested options), respectively, and that Hilrod I sold 5.11% of its holdings. (Compl. ¶ 110).

[27] The Complaint alleges that Kelly held 59,200 shares (including vested options) after his last trade during the Class Period. (Compl. ¶ 110). In fact, Kelly had 17,600 shares remaining. (Ex. MM at 793-95).

history). Further undermining any inference of scienter are the facts that Kelly is not alleged to have made any false or misleading statement and that Kelly's shares represent a tiny percentage (less than 4%) of the total insider sales alleged in the Complaint. *See Vantive*, 283 F.3d at 1094; *Silicon Graphics*, 183 F.3d at 987-88 (no inference of scienter despite insiders' sales of 43.6% and 75.3% of holdings where one insider's sales amounted to only 5% of total sales alleged and other defendant did not make any of the alleged false statements).

(ii) There Is Nothing Suspicious About the Timing of Defendants' Sales

Not a single fact alleged in the Complaint demonstrates that the timing of the Individual Defendants' sales was suspicious or that Defendants timed their sales to "*maximize the personal benefit from undisclosed inside information*." *See Ronconi*, 253 F.3d at 435 (emphasis in original). To the contrary, the facts alleged in the Complaint support the opposite inference.

First, the Individual Defendants cannot even plausibly be said to have sold their shares at an artificially inflated price. (*See* Compl. ¶ 110). The rationale behind the insider trading analysis is that well-timed sales of stock immediately preceding a negative announcement, which results in an insider obtaining a substantial premium over the stock's value following the announcement, raises some inference that the insider may have traded on non-public information. *See Middlesex Ret. Sys. v. Quest Software, Inc.*, 527 F. Supp. 2d 1164, 1185 (C.D. Cal. 2007).

That is demonstrably not the case here. Most of the Individual Defendants' sales – nearly 1.1 million of the roughly 1.6 million shares alleged in the Complaint – were made at prices *below* the average price at which Hansen stock traded between November 9 and the end of the year ($44.80), after the purported "truth" was disclosed. (*See* Compl. ¶ 110; Ex. JJ at 733-34). Moreover, the average closing price ($45.36) during the period in which the Individual Defendants sold (between August 13 and September 14) was essentially the same as the average closing price ($44.80)

between November 9 and the end of the year. (Ex. JJ at 733-37). Where an insider sells stock "at about what the stock was worth after the bad news [became] public, [and] not when they might have gained market advantage from as yet undisclosed bad news," there can be no inference of scienter. *Ronconi*, 253 F.3d at 435.

Second, not only did the Individual Defendants sell stock at roughly the same price that it traded at after the truth allegedly was revealed, but their sales took place *before* the substantial increase in Hansen's stock price that occurred prior to November 8. After the last sale in September the stock price rose. The stock reached a peak close of $68.11 on October 18, 2007, roughly 50% higher than the prices at which the Individual Defendants sold their shares. (Ex. JJ at 734). When, as here, the "insiders miss the boat this dramatically, their sales do not support an inference that they are preying on ribbon clerks who do not know what the insiders know." *Ronconi*, 253 F.3d at 435; *see also Vantive*, 283 F.3d at 1093-94 (fact that stock price continued to increase for several months following the insiders' sales undermines any inference of scienter).

Third, the significant time lapse between the sales at issue and the disclosure that purportedly revealed the "truth" undermines any inference of scienter, because the greater the time lag the less plausible an inference that an inside trade was for the purpose of trying to maximize the personal benefit from undisclosed information. *See Splash Tech. II*, 160 F. Supp. 2d at 1083-84. The first sale on August 13 and the last sale on September 14 were, respectively, nearly three months and two months before the November 8 disclosure that purportedly revealed the truth. *See id.* (trades made four months prior to onset of stock's decline were not "calculated to maximize the personal benefit from undisclosed information" (quoting *Silicon Graphics*, 183 F.3d at 986)); *Head v. NetManage Inc.*, No. C 97-4385, 1998 WL 917794, at *4 (N.D. Cal. Dec. 30, 1998) (sales two months before announcement not suspicious).

Finally, restrictions on the Individual Defendants' ability to trade explain the timing of the Class Period sales. *See, e.g., Ronconi*, 253 F.3d at 436 (noting that "re-

strictions on an insider's ability to trade are important in determining whether the trading pattern is suspicious"). For ten months prior to the first sale, Hansen had been the subject of an informal SEC inquiry that was announced in October 2006. (Ex. F at 122). Hansen announced on August 7, 2007, less than one week before the first sale, that the SEC's investigation had ended without any enforcement action. (Ex. O at 357). Two days later, on Thursday, August 9, 2007, Hansen disclosed its results for the prior quarter. The Individual Defendants' first sale during the Class Period occurred on the following Monday, August 13, 2007. "Trading following public announcements . . . evidences compliance with the securities laws. Indeed, insiders are only permitted to trade in a 'window' after a public announcement is made." *In re Party City Sec. Litig.*, 147 F. Supp. 2d 282, 312 (D.N.J. 2001) (citations omitted); *see also Lipton v. Pathogenesis Corp.*, 284 F.3d 1027, 1037 (9th Cir. 2002) (finding "timing of . . . stock transactions was not suspicious" because "[o]fficers of publicly traded companies commonly make stock transactions following the public release of quarterly earnings and related financial disclosures").

(iii) Defendants' Sales During the Class Period Were Consistent with their Trading Histories

Again, "[i]nsider trading is suspicious only when it is '*dramatically out of line with prior trading practices.*'" *Ronconi*, 253 F.3d at 435 (quoting *Silicon Graphics*, 183 F.3d at 986) (emphasis added). None of the Individual Defendants' sales during the Class Period were out of line with their trading histories, let alone dramatically out of line. Taking into account their stock, vested options, and shares held through entities, Sacks and Schlosberg sold, respectively, 15.56% and 16.41% of their total holdings in the first five months of 2006.[28] Thus, not only were their respective sales

[28] Sacks and Schlosberg are alleged to have sold approximately 940,000 shares each during 2006 (again attributing to each of them 50% of the shares sold by their jointly held entities). (*See* Compl. ¶ 112). Following the last sales on June 2, 2006, Sacks and Schlosberg had remaining a total of 5,100,000 shares and 4,788,776 shares,

of 13.15% and 13.86% during the Class Period consistent with their trading histories, their Class Period sales actually constituted a smaller percentage of their holdings.[29]

Nor are Kelly's sales during the Class Period out of line with his prior sales. Kelly sold 100% of his holdings in 2004, 82.14% of his holdings in 2005, and 92% of his holdings in 2006.[30] (Compl. ¶ 112; Ex. MM at 787-89). Thus, the 77.32% of his holdings that Kelly sold during the Class Period is not only consistent with the percentages of his prior years' trades, but actually lower. In fact, what Kelly's trading history shows is a pattern of his exercising his options and selling the vast majority of the resulting shares in the same year that the options vested, a pattern echoed in his sales during the Class Period. (Compl. ¶¶ 110, 112; Ex. MM at 781-89, 793-95).

Furthermore, the Complaint's allegation that the Individual Defendants' sales during the Class Period were unusually large in comparison to their sales activity during prior years (Compl. ¶ 113) is refuted by the Complaint itself. Sacks, Schlosberg and their entities are collectively alleged to have sold approximately 6.9 million shares in 2004, 1.1 million shares in 2005, 1.9 million shares in 2006 and 1.6 million

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respectively (including shares and vested options held directly and shares held indirectly through Hilrod I and HRS). (Exs. KK at 749-51; LL at 765-67). Notably, and contrary to Plaintiff's allegation that they "unloaded" their Hansen stock during the Class Period (*see* Compl. ¶ 92), Sacks and Schlosberg actually held *more* shares following their 2007 sales than they held following their sales in 2006. *See* note 25, *supra*.

[29] The Complaint's allegation that Sacks and Schlosberg individually sold 8.82% and 9.96%, respectively, of their holdings in 2006 (Compl. ¶ 112) is meaningless because, as noted above, these calculations exclude shares sold and held through Hilrod I and HRS.

The Complaint also sets forth stock sales allegedly made by Hilrod I in 2004 and 2005, but does not even attempt to allege what percentage of Sacks and Schlosberg's overall holdings these sales constituted. (*See* Compl. ¶ 112).

[30] The Complaint's allegation that Kelly sold 69.70% of his holdings in 2006 is incorrect. (Compl. ¶ 112). Kelly retained 4,000 shares (and not 20,000 shares as alleged in the Complaint) after his sales on May 5, 2006. (Ex. MM at 787-89).

shares in 2007. (*See* Compl. ¶¶ 110, 112). Similarly, Kelly is alleged to have sold 128,920 shares in 2004, 46,000 shares in 2005, 46,000 shares in 2006 and 60,000 shares in 2007. (*See id.*). Nothing about this suggests that the Individual Defendants' trading activity in 2007 was in the least suspicious or out of line with their activity in prior years.

4. The Complaint Fails to Plead Loss Causation

The Complaint's allegations of loss causation are also legally insufficient. The PSLRA requires that a plaintiff demonstrate loss causation by showing that "the act or omission of the defendant alleged to violate this title caused the loss for which the plaintiff seeks to recover damages." 15 U.S.C. § 78u-4(b)(4). A plaintiff must "demonstrate a causal connection between the deceptive acts that form the basis for the claim of securities fraud and the injury suffered." *Daou*, 411 F.3d at 1025. To demonstrate such a causal connection, a plaintiff must identify the alleged fraudulent statement that artificially inflated the stock price, as well as the corrective disclosure (*i.e.*, revelation of the truth) that subsequently drove the price down. *Id.* at 1025-27. Stated differently, a plaintiff must sufficiently allege that the market reacted to the disclosure of new facts that revealed a previous representation to have been fraudulent, and not merely to reports of a company's poor financial health generally. *See Metzler*, 540 F.3d at 1063. An allegation that stock was purchased at an inflated price does not establish loss causation. *Dura Pharm. Inc. v. Broudo*, 544 U.S. 336, 347 (2005).

The Complaint alleges that Sacks' statements during a November 8, 2007 earnings call "revealed" the "prior misrepresentations and other fraudulent conduct," and that it was these purported revelations that caused Hansen's stock price to drop. (Compl. ¶¶ 120-23). These allegations fail to plead loss causation because (1) the stock price declined prior to the earnings call and (2) Sacks' statements during the call did not constitute corrective disclosures.

a. The Stock Drop Preceded the November 8, 2007 Earnings Call

On November 7, 2007, Hansen's stock closed at $56.67. (Ex. JJ at 734). The next day, on November 8, 2007, the stock price closed at $43.50, a decline of approximately 23%. (*Id.*). However, the stock price *opened* on the morning of November 8 at an even lower price – $42.86. (*Id.*) The drop between the November 7 close and the November 8 open followed the issuance of a press release announcing Hansen's third-quarter results. (*See* Compl. ¶ 119 (noting that press release was issued prior to market opening on November 8)). The conference call on November 8 had nothing to do with this drop; the call did not start until 2:30 p.m. EST – some five hours after the opening of the market. (Ex. Q at 400-01).

Hansen's stock price, therefore, did not fall after the "truth" was allegedly revealed in the conference call. Indeed, the price rebounded after the conference call. The November 8 closing price of $43.50 was $0.64 cents above the open price of $42.86. (Ex. JJ at 734). A complaint fails to demonstrate loss causation where the stock price declines before the alleged fraud is revealed to the market. *See Daou*, 411 F.3d at 1026-27 (holding that any loss occurring before the alleged disclosure of a prior fraud cannot be considered causally related to that fraud); *Metzler*, 540 F.3d at 1063 (instructing courts to make a "careful delineation between losses caused after the company's [improper] conduct was revealed, and losses suffered before the revelation"). Thus, because Hansen's stock price declined before the earnings call that purportedly revealed the "truth," the Complaint fails to plead a facially plausible theory of loss causation.

b. The November 8, 2007 Earnings Call Was Not a Corrective Disclosure

In any event, none of Sacks' statements during the November 8, 2007 earnings call constituted a disclosure of a prior misrepresentation. The Complaint distorts Sacks' statements and ignores his prior disclosures in a failed attempt to demonstrate loss causation. (Compl. ¶¶ 94, 120-21). *See, e.g., In re Dothill Sys. Corp. Sec. Litig.*,

No. 06-CV-228, 2009 WL 734296, at *14 (S.D. Cal. Mar. 18, 2009) ("[a] disclosing event which does not actually disclose the falsity of the alleged misrepresentations is inadequate" to plead loss causation).

The Complaint alleges that, during the November 8 call, "Defendants disclosed for the first time that they had put the brake on the AB transition . . . because AB was not focusing on Hansen's products." (Compl. ¶¶ 94, 121). But that quote misleadingly splices and combines two innocuous statements. Sacks' comment about putting the brake on the AB transition related solely to the Off-Premise Agreements, and simply reiterated what he had said in prior earnings calls. Regarding the Off-Premise Agreements, Sacks had previously disclosed in a May 14, 2007 call that the transition was "largely done," but that there would still be some markets that would be transitioned at the end of the summer. (Ex. Z at 627). On August 8, 2007, Sacks similarly stated that the off-premise transition was "largely complete" and that Hansen "sort of put a [brake] on some of the transition arrangements during summer," but would "probably continue to do a little bit of transitions after the summer . . . ." (Ex. AA at 635). Thus, Sacks was saying nothing new, let alone revealing a prior fraud, when he again said during the November 8 call that, with respect to the Off-Premise Agreements, "the transition arrangements to the A-B system is largely complete" and "[w]e did put a brake on them," although "[t]here will be some selected markets, where I believe we will continue to transition the additional markets to the A-B system . . . on a carefully selected and determined basis." (Ex. BB at 653).

Nor did Sacks state during the November 8 call that the reason why Hansen put a brake on the AB off-premise transition was that "AB was not focusing on Hansen's products." (Compl. ¶ 94). In fact, Sacks' "focus" comment related solely to the On-Premise Agreement and had nothing to do with the AB Distributors selling in the off-premise markets. (*See* Ex. BB at 654). Further, Sacks did not say (even in relation to the On-Premise Agreement) that AB "was not focusing on distributing Hansen's products." (Compl. ¶ 91). Rather, he stated only that the AB sales team "[have] got

their focus on their own products *as well*" as Hansen's products, and that this posed "some challenges." (Ex. BB at 654) (emphasis added). This statement does not contradict, let alone reveal to be false, anything that Sacks had said previously. Plaintiff does not and cannot allege that Sacks ever represented that AB's sales team was selling Hansen products exclusively (or that the market would ever believe such a representation). Moreover, since announcing the On-Premise Agreement in February 2007, Sacks repeatedly noted the difficulties involved with that agreement, describing it as a "crap shoot" and a "speculative" opportunity that would "take time" to yield results. (Exs. Y at 616-17; AA at 639).

The Complaint also alleges that, during the November 8 call, "Sacks elaborated that AB distributors had not adequately 'embraced the brand and the potential for the brand.'" (Compl. ¶ 121). What Sacks actually said was that "[certain] AB distributors have embraced the brand and potential for the brand in these sort of non-alcoholic accounts more readily with more resources than others" and that, while this has been a challenge, "by and large, we are certainly happy" with the AB transition. (Ex. BB at 653). Moreover, Sacks had previously told the market that there was a "learning curve" for the AB distributors because they were not familiar with distributing nonalcoholic beverages. (Ex. W at 561 ("It takes time. In some of these cases [because] a lot of the distributors haven't [gone through] distributing non-alcoholic products. There is a learning curve.")).

The Complaint also avers that Sacks "disclosed" in the November 8 call that "for independent convenience stores, 'the Budweiser system is not quite as strong' and 'is an area that obviously [Hansen has] to address with the A-B system.'" (Compl. ¶ 121). But this was no corrective disclosure either. What Sacks actually said – in the context of reaffirming that "overall . . . we have increased [our distribution] pretty significantly" through AB – was that "the independents . . . is probably the one area where the Budweiser system is not quite as strong as perhaps, the independent beverage systems like Coke and Pepsi because that's part of their everyday

businesses, going to all these non-alcoholic, small moms and pops, and stores, which are traditionally not on the radar of the beer distributors." (Ex. BB at 653). Moreover, Sacks had told the market back in November 2006 that there were channels "that AB doesn't ordinarily go into" and therefore Hansen would not be able to reach as many accounts. (Ex. W at 577).

Finally, the Complaint highlights that, during the November 8 call, Sacks reported that Allied brands sales had declined in the third quarter of 2007 and had missed internal expectations. (Compl. ¶¶ 94, 120). Sacks' report cannot be deemed a corrective disclosure because it did not contradict (or "correct") a prior report. Indeed, Hansen had not previously announced either actual Allied brand sales data for the quarter or its internal expectations for Allied sales for the quarter. Moreover, as detailed above, Sacks had told the market throughout the Class Period that the Allied brands, particularly Lost, had struggled during the transition to the AB distribution system.

Given that Hansen's stock price dropped before the November 8 earnings call (*i.e.*, the alleged corrective disclosure) and that the November 8 call, in any event, did not reveal any prior fraud, it is clear that the market reacted to Hansen's third quarter 2007 financial results, and not to any alleged revelation of a prior fraud. Accordingly, the Complaint fails to demonstrate loss causation and should be dismissed for this independent reason.

B. The Complaint Fails to State a Claim Under Section 10(b) and Rule 10b-5 for Alleged Insider Trading

The Complaint's second cause of action asserts insider trading claims under section 10(b) and Rule 10b-5 against the Individual Defendants and Hansen.[31] (Compl. ¶¶ 138-45). But this claim adds nothing to the Complaint's first cause of action and should likewise be dismissed.

[31] The insider trading claim against Hansen fails not only for the reasons set forth in the text, but also because Plaintiff does not allege that the Company sold any shares.

A plaintiff asserting an insider trading claim must plead with particularity, as required by the PSLRA and Rule 9(b), that the defendant knowingly traded on the basis of material, non-public information and that the plaintiff traded contemporaneously with the defendant. *See Neubronner v. Milken*, 6 F.3d 666, 669-72 (9th Cir. 1993); *Petco*, 2005 WL 5957816, at *36-37; *Pa. Ave. Funds v. Borey*, No. C06-1737, 2009 WL 902070, at *12-14 (W.D. Wash. Mar. 30, 2009); *Edward J. Goodman Life Income Trust v. Jabil Circuit, Inc.*, 595 F. Supp. 2d 1253, 1287-90 (M.D. Fla. 2009). Thus, Plaintiff must plead particularized facts giving rise to a strong inference of scienter, *i.e.*, that the Defendants intentionally or with deliberate recklessness traded on the basis of material, non-public information. *See Worlds of Wonder*, 35 F.3d at 1427 ("To establish section 10(b) liability . . . the plaintiffs must prove that the insider traders acted with scienter . . . .").

Plaintiff's section 10(b) insider trading claim is based on the exact same deficient allegations that fail to state a section 10(b) misrepresentation claim. The only putatively material, non-public information alleged in the Complaint relates to Sacks' statements about the AB system, the Allied brands, and Hansen's second quarter 2007 financial results. As explained above, the Complaint fails to plead particularized facts showing that any of these statements were false or that the Individual Defendants knew they were false. Indeed, the problems that Plaintiff alleges rendered the AB system and Allied brand statements false were publicly disclosed throughout the Class Period. Because Plaintiff fails to plead with particularity that material, non-public information even existed, much less that the Individual Defendants knowingly traded based on such information, Plaintiff's insider trading claim should be dismissed. *See In re Gap Sec. Litig.*, No. C-87-4895, 1988 WL 168341, at *8 (N.D. Cal. Sept. 28, 1988) (dismissing insider trading claim that was based on same factual allegations underlying plaintiffs' deficient misrepresentation claim).

There is an additional reason why Plaintiff's insider trading claim fails. "[T]he scope of liability for insider trading claims under section 10(b) and Rule 10b-5 is con-

fined to persons who traded contemporaneously with the insider." *Neubronner*, 6 F.3d at 670. "[P]laintiff must have traded in a company's stock at about the same time as the alleged insider." *Brody v. Transitional Hosps. Corp.*, 280 F.3d 997, 1001 (9th Cir. 2002). "Generally this has meant that the trades must occur within a few days of each other." *Middlesex Ret. Sys. v. Quest Software, Inc.*, No. CV 06-6863, 2008 WL 7084629, at *14 (C.D. Cal. July, 10, 2008). Here, Plaintiff alleges that it purchased its Hansen stock on October 25, 2007 – 73 days after the first of the Individual Defendants' sales on August 13, and 41 days after the last sale on September 14. (*See* Ex. B to Decl. of Ramzi Abadou in Support of Structural Ironworkers Local Union #1 Pension Fund's Motion for Consolidation, Appointment as Lead Plaintiff and Approval of Its Selection of Lead Counsel). Therefore, Plaintiff lacks standing to assert an insider trading claim because it did not trade contemporaneously with any of the Individual Defendants, and accordingly the insider trading claims should be dismissed.[32]

C. The Complaint Fails to State a Claim Under Section 20(a) for Control Person Liability

Plaintiff also brings claims against the Defendants under Section 20(a) of the Exchange Act for control person liability. A *prima facie* case under Section 20(a) requires (1) "a primary violation of federal securities law" and (2) the exercise of "actual power or control [by the defendant] over the primary violator." *Zucco Partners*, 552 F.3d at 990; *Howard v. Everex Sys., Inc.*, 228 F.3d 1057, 1065 (9th Cir. 2000). As explained above, Plaintiff has failed to allege a viable claim under Section 10(b) against the Company or any of the Defendants. Accordingly, Plaintiff's Section 20(a) claim fails at the threshold. *See Zucco Partners*, 552 F.3d at 990.

Even if Plaintiff had adequately pled a primary violation under Section 10(b), which

[32] In addition, Plaintiff's claim fails because the Complaint is devoid of any allegations sufficient to establish a causal connection between the Individual Defendants' sales and any losses allegedly sustained by Plaintiff.

it has not, its Section 20(a) claim still would fail because of Plaintiff's failure to allege facts concerning the critical element of control. Plaintiff must establish "control" by demonstrating that the defendants exercised actual control in an effort to induce violations of securities laws. *In re Downey Sec. Litig.*, No. CV 08-3261, 2009 WL 2767670, at *15 (C.D. Cal. Aug. 21, 2009). The Complaint generally alleges that, "[b]y virtue of their position and their power to control public statements about Hansen, the defendants had the power and ability to control the actions of Hansen and its employees." (Compl. ¶ 147). Such boilerplate assertions are insufficient to state a claim for control person liability. *See Downey*, 2009 WL 2767670, at *15 (dismissing plaintiff's Section 20(a) claims because plaintiff did not make "particularized allegations that the Individual Defendants exercised control . . . in an effort to induce [primary violators] to engage in acts that violated the securities laws" nor state "the times, dates, and places that such control allegedly occurred"). It cannot be automatically assumed that Defendants are controlling persons under Section 20(a). *See id.* Yet Plaintiff does not set forth any facts to establish the Defendants' "control." Thus, the Section 20(a) claim should be dismissed.[33]

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[33] The Complaint asserts a Section 20(a) claim against Hansen, but Hansen is outside the scope of that section. *See Hollinger v. Titan Capital Corp.*, 914 F.2d 1564, 1577 (9th Cir. 1990) (noting that § 20(a) "was intended to impose liability on . . . controlling shareholders and corporate officers, who would not be liable under respondeat superior because they were not actual employers").

IV. CONCLUSION

For the foregoing reasons, the Consolidated Complaint should be dismissed in its entirety, with prejudice, and without leave to replead.

DATED: November 16, 2009

Respectfully submitted,

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